



**DEPARTMENT OF INSURANCE, FINANCIAL
INSTITUTIONS AND PROFESSIONAL REGISTRATION**

P.O. Box 690, Jefferson City, Mo. 65102-0690

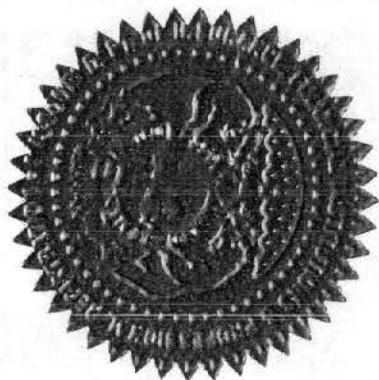
RE: Examination Report of Blue Cross and Blue Shield of Kansas City as of December 31, 2007

ORDER

After full consideration and review of the report of the financial examination of Blue Cross and Blue Shield of Kansas City for the period ended December 31, 2007, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, Linda Bohrer, Acting Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 374.205.3(3)(a), RSMo., adopt such report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, the findings and conclusions of the examination report are incorporated by reference and deemed to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo.

Based on such findings and conclusions, I hereby ORDER Blue Cross and Blue Shield of Kansas City, to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed by such report: (1) implement, and verify compliance with, each item mentioned in the General Comments and/or Recommendations section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions.

So ordered, signed and official seal affixed this December 30, 2008.



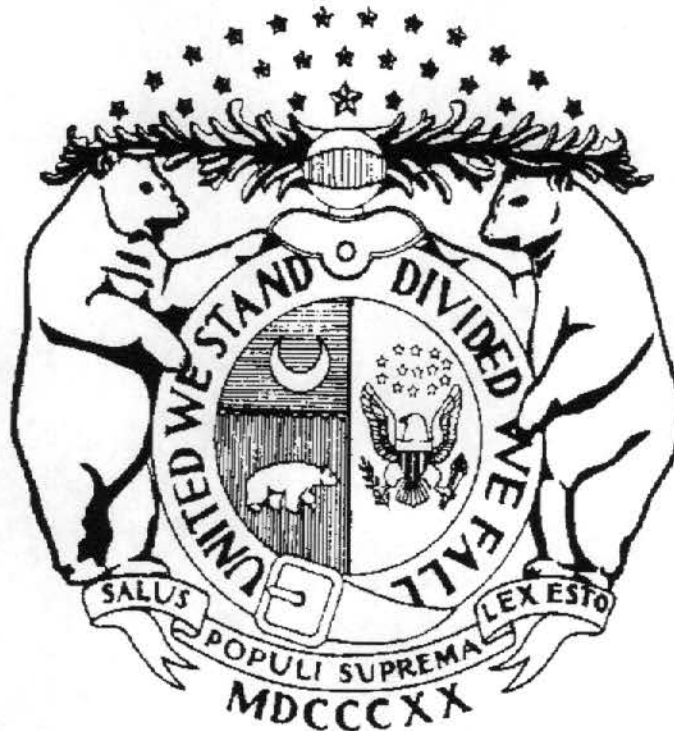
Linda Bohrer

Linda Bohrer, Acting Director
Department of Insurance, Financial Institutions
and Professional Registration

REPORT OF THE
ASSOCIATION FINANCIAL EXAMINATION OF
BLUE CROSS AND BLUE SHIELD
OF KANSAS CITY

AS OF
DECEMBER 31, 2007

FILED
JAN 09 2009
DIRECTOR OF INSURANCE,
FINANCIAL INSTITUTIONS &
PROFESSIONAL REGISTRATION



STATE OF MISSOURI
DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS
AND PROFESSIONAL REGISTRATION
JEFFERSON CITY, MISSOURI

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Kansas City, Missouri
November 10, 2008

Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance
Chairman, (E) Financial Condition Committee, NAIC

Honorable Merle Scheiber, Commissioner
South Dakota Division of Insurance
Midwestern Zone Secretary

Honorable Linda Bohrer, Acting Director
Missouri Department of Insurance, Financial
Institutions and Professional Registration
301 West High Street, Room 530
Jefferson City, Missouri 65102

Ladies and Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

Blue Cross and Blue Shield of Kansas City

hereinafter referred to as such, as BCBS of Kansas City, or as the Company. Its administrative office is located at 2301 Main Street, Kansas City, Missouri 64108, telephone number 816-395-2222. This examination began on April 28, 2008 and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The prior full scope association financial examination of BCBS of Kansas City was made as of December 31, 2004 and was conducted by examiners from the States of Missouri and Kansas representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC) with no other Zones participating.

The current full scope association financial examination covered the period from January 1, 2005 through December 31, 2007 and was conducted by examiners from the States of Missouri and Kansas, representing the Midwestern Zone of the NAIC.

This examination was conducted concurrently with the examinations of the Company's insurance subsidiaries, Good Health HMO, Inc. d/b/a Blue Care, Inc. (Good Health), Blue Advantage Plus of Kansas City, Inc. (BA+) and Missouri Valley Life and Health Insurance Company (Missouri Valley).

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) and statutes of the State of Missouri prevailed.

The examiners relied upon tests of controls, narrative descriptions, fraud risk assessment and other information supplied by the Company's independent auditor, Ernst & Young, LLP, of Kansas City, Missouri, for its audit covering the period from January 1, 2007 through December 31, 2007.

Comments - Previous Examination

The comments, recommendations, and notes of the previous financial examination report dated as of December 31, 2004 are listed below with the subsequent response or action taken by the Company in regard to such comments, recommendations, and notes:

Ancillary Provider Network Agreement

Comment: The Company amended the Ancillary Provider Network Agreement many times and changed the list of parties to the agreement without filing a Form D for prior approval from the DIFP as required by Section 382.195 RSMo (Prohibited transactions, exceptions). The Company was directed to submit a Form D filing for these changes.

Company's Response: The Company revised this agreement to incorporate all previous amendments and other desired revisions. A Form D filing was submitted for approval with the revised agreement.

Current Findings: The Company submitted a revised agreement incorporating all amendments to the DIFP for approval in 2006.

Administrative Services Agreements

Comment: The Company was not in compliance with the payment and settlement procedures outlined in the Administrative Services Agreements with Good Health and Missouri Valley (Agreements). The Agreements specify payment for the previous month's services should be received by the 15th of the subsequent month. Instead of billing for the services under these agreements as stipulated, BCBS of Kansas City combined the settlement with that of the Agreement for the Management of Intercompany Payables and Receivables, which was generally settled quarterly with an imputed interest. The Company was directed to abide by the settlement periods in the Agreements or amend the Agreements to change the payment and settlement periods.

Company's Response: The Company has amended the Administrative Services Agreements to provide for settlements to occur quarterly and has submitted a Form D to the DIFP for approval.

Current Findings: The Company submitted restated Administrative Service Agreements effective August 1, 2006. The new agreements require quarterly settlements.

Lease Agreement

Comment: BCBS of Kansas City entered into a lease agreement with a subsidiary property company, for its home office. For the entirety of the lease term, BCBS of Kansas City did not pay the agreed upon rent per the lease terms. The Company was directed to follow payment and settlement terms in all agreements entered into with subsidiaries and affiliates.

Company's Response: The lease agreement between the Company and Group Health Property Company of Kansas City, LLC. (Group Health Property) was terminated effective September 15, 2005. If the Company enters into such leases in the future, it will comply with the payment terms of such leases.

Current Findings: The lease agreement was terminated September 15, 2005 when BCBS of Kansas City acquired its home office building upon the dissolution of the Group Health Property.

Agreement for Intercompany Payables and Receivables

Comment: BCBS of Kansas City was not settling balances under this agreement on a consistent manner. The Company also combined balances from unrelated agreements with subsidiaries to the settlement terms under this agreement. The Company was directed to amend the Agreement for the Management of Intercompany Payables and Receivables to include specific settlement terms by filing a Form D with the DIFP in accordance with RSMo 395.182 (Prohibited transactions, exceptions). The Company was also directed to desist from including other intercompany balances in the calculation of interest under the agreement.

Company's Response: The Company amended the Agreement for Intercompany Payable and Receivables to provide for settlement to occur quarterly and has submitted a Form D to the DIFP. The amendment also provides for interest calculations on balances arising from the agreement itself, as well as balances arising from other intercompany agreements specifically identified.

Current Findings: The Company submitted a restated Agreement for Management of Intercompany Payables and Receivables effective August 1, 2006. The new agreement requires settlement 90 days after receipt of funds, and specifically includes the management of balances related to the Administrative Agreements.

Collaboration Agreement

Comments: The predecessor name of Preferred Health Professionals, LLC was still listed on this agreement, although the name change occurred on September 27, 2004. The Company was directed to draft an amendment reflecting the name change and submit a Form D filing for this amendment, as required by Section 382.195 RSMo (Prohibited Transactions, Exceptions).

Company's Response: Preferred Health Professionals, LLC is the successor organization of the corporation, Preferred Health Professionals. By operation of law, the merger of the predecessor corporation into the limited liability company made the new LLC entity a party to the contract its predecessor had signed without the need to change the name of the contracting party on the agreement. Nevertheless, the Company will draft an amendment to reflect the name change and submit a Form D to the DIFP.

Current Findings: The Company submitted a restated Collaborative Agreement effective January 1, 2006.

Administration Agreement

Comment: The Administration Agreement between BCBS of Kansas City and EPOCH on behalf of Missouri Valley overlapped in functionality with the Agreement for the Management of Intercompany Payables and Receivables between BCBS of Kansas City and Missouri Valley. The Company was directed to amend the Agreement for the Management of Intercompany Payables and Receivables and the Administration Agreement to specifically state that EPOCH is collecting premiums and paying claims only for Missouri Valley's direct pay PPO product.

Company's Response: The Company will amend the Agreement for Intercompany Payables and Receivables to explicitly state that the services provided by the Company to Missouri Valley will not include the receipt of premiums and payment of claims for the Missouri Valley direct pay PPO product.

Current Findings: The Company submitted a restated Agreement for Management of Intercompany Payables and Receivables effective August 1, 2006.

Transaction with Pharma-Link, Inc.

Comment: The Company provided administrative services to its wholly owned subsidiary, Pharma-Link, Inc. (PLI). These services were not covered under an intercompany agreement and were not being accounted for on the Company's or PLI's general ledgers. The Company also did not disclose its ownership of PLI on Schedule Y - Part 1 of the Annual Statement. The Company was directed to draft an agreement and submit a Form D to the DIFP for services provided to PLI, in accordance with RSMo 382.195 (Prohibited transactions, exceptions). In addition, services that qualify as management services were to be reported on Schedule Y - Part 2 of the Annual Statement.

Company's Response: Pharma-Link was dissolved in 2006. In the future the Company will ensure that agreements are in place with all subsidiaries for which the Company provides services. The Company will also ensure services qualifying as management services are reported on Schedule Y – Part 2 of the Annual Statement.

Current Findings: The prior comment no longer applies due to the dissolution of Pharma-Link.

Ceded Reinsurance Agreement

Comment: The Company failed to file a ceded reinsurance agreement between itself and BCS Insurance Company with the DIFP within 10 days of execution pursuant to Missouri Regulation, 20 CSR 400-7.140 (2), Health Maintenance Organizations - Reinsurance Agreements. The Company was directed to comply with this regulation.

Company's Response: When agreements are reached with the reinsurer, the Company executes the documents first and then forwards them to the reinsurer to sign per the reinsurer's instruction. The Company sent copies of the fully executed agreement to the DIFP the day after it was received from the reinsurer.

Current Findings: Reinsurance agreements were timely filed during the period under examination.

Cash and Short-term Investment Receivable from Parent, Subsidiaries and Affiliates

Comment: The account balances reported by the Company for the above Annual Statement line items were adjusted to correct improper reporting and classification arising from related party transactions. The Company was directed to report the effect of its agreement with related parties in the appropriate lines of the Annual Statement.

Company's Response: In the future, the Company will properly report amounts due and payable to BCBS of Kansas City as Amounts Due to Parent, Subsidiaries and Affiliates and not report these amounts as Cash.

Current Findings: The Company properly reported amounts due and payable under its intercompany agreements for the period under exam.

HISTORY

General

Blue Cross and Blue Shield of Kansas City was created from the merger of Blue Cross of Kansas City and Blue Shield of Kansas City in 1982. Blue Cross of Kansas City was established in 1938 to provide hospital insurance. Blue Shield of Kansas City was established in 1943 to provide insurance for physician fees. BCBS of Kansas City was incorporated on May 17, 1982 as a not-for-profit health services corporation, under the laws of Chapter 354 RSMo (Health Services Corporations sections).

In 1995, the BCBS of Kansas City obtained a license to also operate as a health maintenance organization (HMO), under the laws of Chapter 354 RSMo (Health Maintenance Organization sections).

Capital Stock

The Company is a not-for-profit entity. Therefore, there is no capital stock ownership.

Dividends

Due to the Company's not-for-profit status, no dividends or cash distributions have been made or declared since incorporation.

Management

The management of BCBS of Kansas City is vested in a Board of Directors. The Company's Bylaws specify that the number of directors shall be no fewer than twelve (12) and no more than sixteen (16). As of December 31, 2007, fifteen (15) directors were serving on the Board. The directors were comprised primarily of physicians, business leaders, and community leaders in the Kansas City, Missouri metropolitan area. The Board of Directors appointed and serving as of December 31, 2007, were as follows:

Name and Address

Business Affiliation

Tom E. Bowser
Olathe, Kansas

President and CEO, BCBS of Kansas City

Randall C. Ferguson, Jr.
Lee's Summit, Missouri

Retired Executive, IBM Corporation
Director, Great Plains Energy
Former Senior Partner, Tshibanda & Associates, LLC

Melvin L. Glazer, MD
Overland Park, Kansas

Secretary of the Board of Directors, BCBS of Kansas City
Physician, Kansas City Medical Group

Henry J. Herrmann
Olathe, Kansas

CEO, Waddell & Reed Financial, Inc.

Karon E. Harris Hicks
Lake Ozark, Missouri

Retired BCBS of Kansas City Executive

Garry K. Kemp
Lee's Summit, Missouri

Business Manager, Greater Kansas City Building
and Construction Trades Council

Janice C. Kreamer
Kansas City, Missouri

Vice Chairman of the Board, BCBS of Kansas City
Former President, Greater Kansas City Community
Foundation

Thomas A. McCullough
Overland Park, Kansas

EVP, COO and Director, DST Systems, Inc.
Director, Carondelet Health
Retired Partner, Ernst and Young

Michael F. Morrissey
Leawood, Kansas

Retired Managing Partner, Ernst and Young
Director, J.E. Dunn Construction Group, Inc.

William C. Nelson
Mission Hills, Kansas

Chairman of the Board, BCBS of Kansas City
Chairman, George K. Baum Asset Management
Director, Great Plains Energy
Director, DST

Lyle K. Querry
Independence, Missouri

Former Business Manager, International Brotherhood
of Electrical Workers

Sam R. Reda
Olathe, Kansas

Retired Executive, Lockton Benefit Company

James R. Roath
Marco Island, Florida

President, J.S. Roath Investment Corporation

Lawrence A. Rues, MD
Kansas City, Missouri

Emeritus Director and Faculty, Research Family Medicine
Residency, Physician Research Medical Center

Marilyn M. Rymer, MD
Shawnee Mission, Kansas

Medical Director, Mid America Brain & Stroke Institute,
St. Luke's Hospital

Committees

The Bylaws provide for the Board of Directors to appoint six committees annually. As of December 31, 2007, the members of each committee were as follows:

Executive Committee

William C. Nelson, Chairman
Tom E. Bowser, CEO
Melvin L. Glazer, M.D.
Karon Harris Hicks
Janice C. Kreamer
Tom A. McCullough
Michael F. Morrissey
Lawrence A. Rues, M.D.

Governance Committee

Lyle K. Querry, Chairman
Karon Harris Hicks
Sam R. Reda
Lawrence A. Rues, M.D.
Randall C. Ferguson, Jr.
Marilyn M. Rymer, M.D.

Audit Committee

Michael F. Morrissey, Chairman
Randall C. Ferguson, Jr.
Henry J. Herrmann
Garry K. Kemp
Thomas A. McCullough
James R. Roath

Personnel Committee

Karon Harris Hicks, Chairman
Melvin L. Glazer, M.D.
Garry K. Kemp
L. Keith Querry
Sam R. Reda
James R. Roath
Lawrence A. Rues, M.D.

Investment Committee

Thomas A. McCullough, Chairman
Henry J. Herrmann
Janice C. Kreamer
Michael F. Morrissey
James R. Roath

Health Policy and Quality Committee

Lawrence A. Rues, M.D., Chairman
Melvin L. Glazer, M.D.
Janice C. Kreamer
Lyle K. Querry
Sam R. Reda
Marilyn M. Rymer, M.D.

Officers

The Board of Directors annually elects various Company officers, as required by the Bylaws. The senior officers elected and serving as of December 31, 2007, were as follows:

Tom E. Bowser	President and Chief Executive Officer
John W. Kennedy	Executive Vice President and Chief Operating Officer.
Peter K. Yelorda	Executive Vice President and Chief Administrative Officer
Roger L. Foreman	Executive Vice President and Chief Marketing Officer.
David R. Gentile	Executive Vice President and Chief Member Services & Subsidiaries Officer
Marilyn T. Tromans	Vice President, Chief Financial Officer and Treasurer
Blake J. Williamson	Vice President and Senior Medical Director Care Management
Richard J. Kastner	Vice President and General Counsel
Sharon I. O'Connor	Manager, Board Relations and Corporate Secretary

Conflict of Interest

The Company has implemented a conflict of interest policy, which establishes procedures for the disclosure of any conflicts of interest that may exist. All officers and directors are required to complete a conflict of interest statement annually. Signed statements of officers and directors were reviewed for the examination period. No significant exceptions were disclosed.

Corporate Records

The Company's Articles of Consolidation and Incorporation and Bylaws were reviewed for the period under examination. The Articles of Consolidation and Incorporation were not amended during the examination period. The Bylaws were amended on May 16, 2007 to revise various committee functions and responsibilities. The amendment also created an Investment Committee which is responsible for investment policy, guidance and oversight.

The minutes of the Board of Directors meetings and the committee meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

Acquisitions, Mergers and Major Corporate Events

Several changes to the subsidiaries of BCBS of Kansas City occurred during the examination period, as follows:

- April 18, 2005 – Blue Advantage Plus of Kansas City, Inc., was incorporated as a wholly owned subsidiary to operate as an HMO, specializing in Title XIX Medicaid business.
- November 28, 2005 - BCBS of Kansas City acquired the remaining 50% ownership interest in EPOCH, a third party administrator licensed in the State of Missouri. After the acquisition of EPOCH, the Company contributed 1% of its ownership interest to Good Health HMO, Inc.
- On August 18, 2003, BCBS of Kansas City purchased its current home office building located at 2301 Main, Kansas City, Missouri. BCBS of Kansas City formed a subsidiary called Group Health Property Company of Kansas City, LLC to own the home office property and then to lease it back to the Company. On September 15, 2005, Group Health Property was liquidated and the lease terminated. Group Health's sole asset, the home office building, was transferred back to the Company. The carrying value of the home office building at the time of Group Health Property's dissolution was \$21,187,088.

Surplus Debentures

No surplus debentures were issued or outstanding as of December 31, 2007.

AFFILIATED COMPANIES

Holding Company, Subsidiaries and Affiliates

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by BCBS of Kansas City on behalf of itself and its subsidiaries for each year of the examination period.

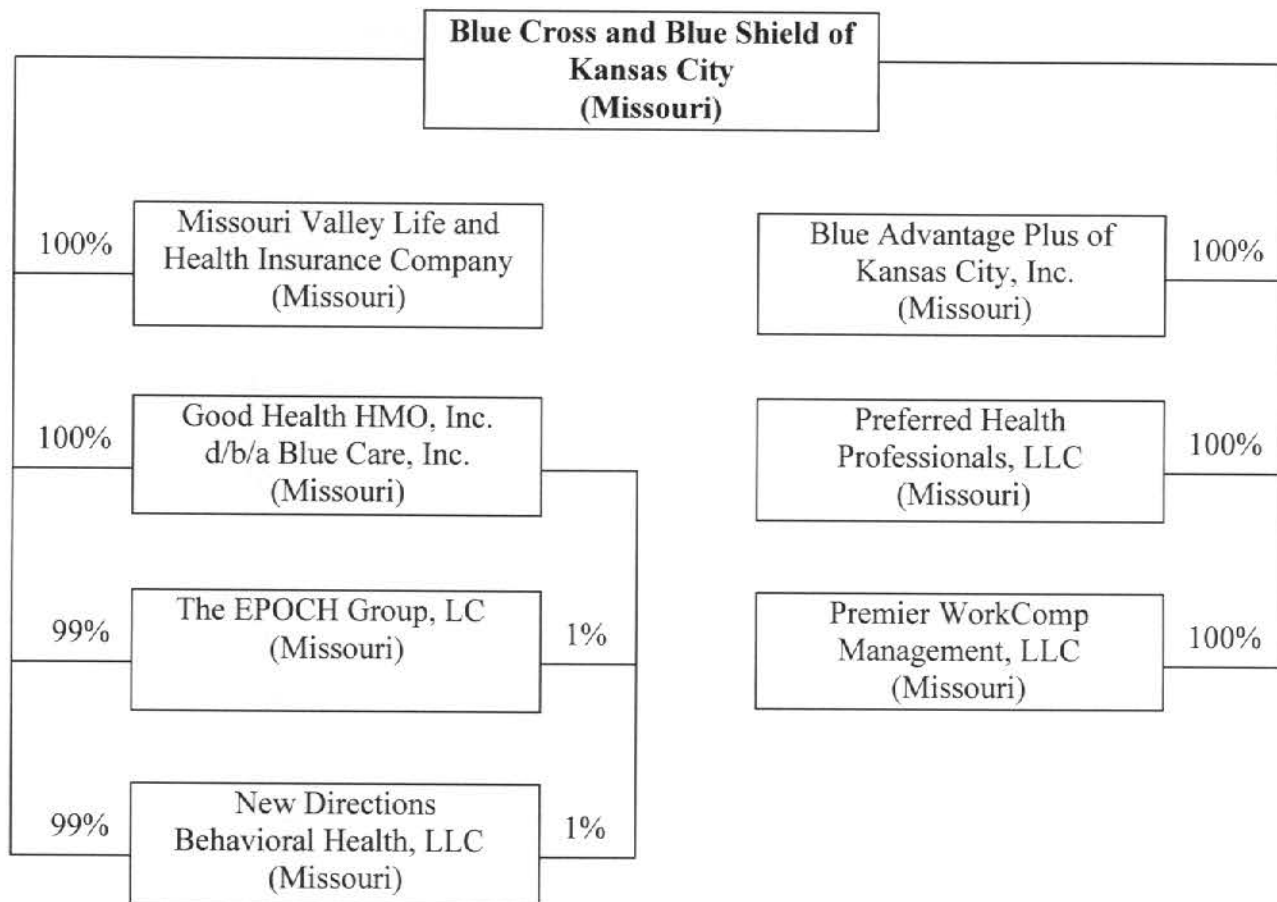
The Company is a not-for-profit organization and therefore, there are no stockholders or other ownership. BCBS of Kansas City is ultimately controlled by its Board of Directors.

BCBS of Kansas City has several subsidiaries that all have businesses involved in or related to the health care industry. These subsidiaries are described as follows:

- Good Health HMO, Inc. d/b/a Blue Care, Inc., Blue Advantage Plus of Kansas City, Inc., and Missouri Valley Life and Health Insurance Company are Missouri domiciled insurers.
- The EPOCH Group, LC provides administrative services for third-party employers that have self-funded health insurance programs.
- Preferred Health Professionals, LLC (PHP) provides network rental and managed care services to groups, third-party claims administrators and insurance companies.
- Premier WorkComp Management, LLC (PWC) provides clients with access to a provider network exclusively for the treatment of work-related injuries and illnesses.
- New Directions Behavioral Health, LLC (New Directions) manages behavioral health benefits and provides employee assistance programs for its customers.

Organizational Chart

The following organizational chart depicts BCBS of Kansas City's ownership and holding company system, as of December 31, 2007:



Intercompany Transactions

The Company's intercompany agreements in effect, as of December 31, 2007, are outlined below.

1. **Type:** Agreement for the Sharing of Federal Income Taxes and Filing of a Consolidated Tax Return

Affiliates: Good Health, Missouri Valley, BA+, Pharma-Link, Inc.

Effective: November 1, 2005

Terms: BCBS of Kansas City will file a consolidated federal tax return for itself and its subsidiaries. The tax liability for each subsidiary shall be based upon each subsidiary's taxable income or loss as reflected in the consolidated financial statements. Each subsidiary will pay its federal income taxes to BCBS of Kansas City. BCBS of Kansas City will collect and remit any tax refunds to the subsidiaries.

This agreement was terminated, and a new agreement was signed effective January 3, 2008. The only difference between the two agreements was the removal of Pharma-Link, Inc. as a party to the agreement.

2. Type: Administrative Services Agreement

Affiliate: Missouri Valley

Effective: August 1, 2006

Terms: BCBS of Kansas City agrees to provide the following administrative services: accounting, budgeting, personnel, payroll, office space, utilities, maintenance, claims processing, purchasing, legal, actuarial, underwriting, cash management, investment, marketing, data processing, and other services. Missouri Valley will pay BCBS of Kansas City the actual expenses incurred for the services provided.

3. Type: Administrative Services Agreement

Affiliate: Good Health

Effective: August 1, 2006

Terms: BCBS of Kansas City agrees to provide the following administrative services: accounting, budgeting, personnel, payroll, office space, utilities, maintenance, claims processing, purchasing, legal, actuarial, underwriting, cash management, investment, marketing, data processing, and other services. Good Health will pay BCBS of Kansas City the actual expenses incurred for the services provided.

4. Type: Administrative Services Agreement

Affiliate: BA+

Effective: August 1, 2006

Terms: BCBS of Kansas City agrees to provide the following administrative services: accounting, budgeting, personnel, payroll, office space, utilities, maintenance, claims processing, purchasing, legal, actuarial, underwriting, cash management, investment, marketing, data processing, and other services. BA+ will pay BCBS of Kansas City the actual expenses incurred for the services provided.

5. Type: Management Services Agreement

Affiliates: Premier WorkComp

Effective: January 1, 2003

- Terms:** BCBS of Kansas City will provide the following support and management services to PWC: office space; phone system; receptionist; office supplies; copying, printing, fax, and mail; office furniture and equipment; internet/intranet activity; accounting; personnel and personnel support; legal services; and information technology and services. PWC will pay BCBS of Kansas City for the actual cost of providing the aforementioned expenses.
6. **Type:** Collaboration Agreement
- Affiliate:** PHP
- Effective:** January 1, 2003; amended December 23, 2004; amended June 28, 2006 (name change from PHP, Inc. to PHP, LLC)
- Terms:** BCBS of Kansas City grants PHP the right to market and sell access to its networks. PHP will pay BCBS of Kansas City an access fee of \$7.50 per enrolled employee of each group per month of the Freedom Network and Freedom Network Select. BCBS of Kansas City agrees to make available certain managerial and administrative employees to PHP. PHP will reimburse BCBS of Kansas City for the expenses of the loaned employees.
7. **Type:** Ancillary Provider Network Agreement
- Affiliates:** New Directions, Good Health, Blue-Advantage Plus of Kansas City, Missouri Valley
- Effective:** January 1, 2006; amended October 1, 2007
- Terms:** New Directions agrees to manage and/or arrange for the provision of behavioral health and substance abuse services for BCBS of Kansas City's members and the members of BCBS of Kansas City's subsidiaries. New Directions will provide for the credentialing reviews of the providers. BCBS of Kansas City will pay New Directions a capitation payment each month that is determined by the per member/per month rates specified in the agreement. The rates vary between products sold by BCBS of Kansas City and its subsidiaries.
8. **Type:** Agreement for the Management of Intercompany Payables and Receivables
- Affiliates:** Missouri Valley, Good Health, BA+
- Effective:** August 1, 2006
- Terms:** BCBS of Kansas City shall pay the payables and collect the receivables for its subsidiaries. Separate accounting records will be maintained for the transactions for each subsidiary. Transfers of funds to or from the subsidiaries will be made to minimize uninvested cash balances and to minimize the receivable or payable balance with each subsidiary.

BCBS of Kansas City shall pool and retain the consolidated funds resulting from these transactions and invest the pooled funds. BCBS of Kansas City shall pay interest or receive interest each month from the subsidiaries based on the intercompany balance of each subsidiary. The interest rate shall be the applicable federal rate determined by the most recently published Internal Revenue Service in a Revenue Ruling.

Exception: The Agreement for the Management of Intercompany Payables and Receivables contradicts the Medicaid Agreement between BA+ and the State of Missouri. The Medicaid Agreement requires direct payment of premiums to BA+'s bank account while the Agreement for the Management of Intercompany Payables and Receivables gives BCBS of Kansas City the authority to collect all premiums. The Company is directed to amend the Agreement for the Management of Intercompany Payables and Receivables to exclude the Medicaid premium portion paid directly to BA+ from BCBS of Kansas City's authority to receive the subsidiary's remaining receivables. The amendment should be filed with DIFP in accordance with Section 382.195 RSMo (Prohibited transactions, exceptions).

9. Type: Administration Agreement

Affiliate: EPOCH

Effective: January 1, 2005

Terms: EPOCH agrees to provide claim processing/payment and premium billing/collecting for Missouri Valley's health PPO product. Missouri Valley is not a party of this agreement. Prior to January 1, 2005, BCBS of Kansas City covered these services under the Administrative Services Agreement and the Agreement for the Management of Intercompany Payables and Receivables.

Exception: As part of its move into a separate office building, EPOCH is reimbursing BCBS of Kansas City for certain administrative expenses. The reimbursement of these expenses is not addressed in the Administration Agreement. The Company should amend the current Administration Agreement to include the expense reimbursements or enter into a separate agreement with EPOCH that address the reimbursements. The amendment or new agreement should be filed with the DIFP as required by Section 382.195 RSMo (Prohibited Transactions, Exceptions).

10. Type: Health Management Agreement

Affiliate: New Directions Behavioral Health, Good Health

Effective: April 1, 2007

Terms: New Directions agrees to provide health coaching services to BCBS of Kansas City and Good Health members, as detailed in the agreement. New Directions is to be paid a fee of \$90 per member for provision of these services. Fees are to be billed on a monthly basis and are due 30 days after the billing date.

11. Type: Guarantor Agreement

Affiliate: Missouri Valley

Effective: March 1, 1991

Terms: BCBS of Kansas City agrees to provide any contributions to the capital and surplus of Missouri Valley necessary to maintain capitalization of \$1,500,000.

12. Type: Guarantor Agreement

Affiliate: Good Health

Effective: January 1, 1993

Terms: In the event of the insolvency of Good Health, BCBS of Kansas City agrees to provide Good Health whatever guarantee or coverage necessary to meet all applicable requirements of its business as a state-qualified HMO. This coverage will provide for the continuation of covered benefits to Good Health's members and pay provider expenses, as defined in the agreement.

13. Type: Guarantor Agreement

Affiliate: BA+

Effective: July 1, 2005

Terms: In the event of the insolvency of BA+, BCBS of Kansas City agrees to provide BA+ whatever guarantee or coverage that is necessary to meet all applicable requirements of its business as a state-qualified HMO. This coverage will provide for the continuation of covered benefits to BA+'s members and pay provider expenses, as defined in the agreement.

In addition to the agreements noted above, the Company also had the following other intercompany transactions during the period under examination:

BCBS of Kansas City has a group term life insurance policy issued by its subsidiary, Missouri Valley. This policy provides a \$5,000 death benefit for members enrolled in the Company's Preferred Care Blue and Blue Advantage individual health products. The life insurance premium is \$1.50 per month for each insured life. BCBS of Kansas City pays premiums to Missouri Valley for the Company's eligible members.

The Company made various capital contributions to various affiliates over the course of the examination. These amounts are detailed below in the Intercompany Payments section of this report.

During 2005, the Company made a \$4,125,161 loan to EPOCH, related to the buyout of the 50% interest of EPOCH owned by a third party. During 2007, the Company made an additional loan to EPOCH in the amount of \$1,620,931.

Intercompany Payments

The following table summarizes the net amounts (received) and paid during the examination period, between BCBS of Kansas City and its subsidiaries.

	2007	2006	2005
Agreement for Sharing Federal Income Taxes			
(Received) from/paid to BCBS of Kansas City	(1,377,810)	1,668,915	35,600
Administrative Services Agreement - Missouri Valley			
Received from Missouri Valley	(65,893)	(79,513)	(260,398)
Administrative Services Agreement - Good Health			
Received from Good Health	(32,591,375)	(24,860,913)	(24,228,123)
Administrative Services Agreement - BA+			
Received from BA+	(10,816,385)	(9,985,710)	(4,390,427)
Management Services Agreement			
Received from PWC	(740,880)	(785,420)	(831,507)
Collaboration Agreement			
Received from PHP	(12,870,093)	(12,811,361)	(14,093,169)
Ancillary Provider Network Agreement			
Paid to New Directions	5,783,755	6,958,245	8,562,524
Management of Intercompany Payables/Receivables			
Received from various subsidiaries	(286,363)	(242,277)	(158,013)
Administrative Agreement			
Paid to EPOCH	41,622	78,023	104,493
Health Management Agreement			
Paid to New Directions	2,643	-	-
Term Life Insurance Policy			
Paid to Missouri Valley	964,578	958,851	919,599
Capital Contributions			
Paid to BA+	4,700,000	4,500,000	8,000,000
Paid to Good Health	-	3,000,000	35,931
Net amount paid or (received)	(47,256,201)	(31,601,160)	(26,303,490)

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured along with its subsidiaries on a financial institution bond. The bond provides fidelity coverage with a liability limit of \$10 million and a deductible of \$150,000. This coverage complies with the suggested minimum amount of fidelity insurance, according to NAIC guidelines.

The Company is also a named insured on the following insurance policies: commercial general liability, umbrella excess liability, commercial auto, commerce liability/business loss, computer crime, errors and omissions, directors and officers liability, fiduciary liability and employment practices.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

As of December 31, 2007, the Company had approximately 1,000 employees. The employees work on the operations of BCBS of Kansas City and its various subsidiaries. Employee benefit costs are allocated to the subsidiaries, pursuant to agreements that are described in the Intercompany Transactions section of this report. A variety of standard benefits are provided to the employees. These benefits include, but are not limited to, health insurance, dental insurance, disability insurance, life insurance, tuition reimbursement, and a 401(k) savings plan with matching contributions.

All vested employees are covered by a qualified, defined benefit pension plan that is managed by the Blue Cross and Blue Shield Association National Retirement Program. There are executives whose pension benefits under the qualified plan are reduced due to statutory limitations on earnings and benefits. These executives are provided with a non-qualified, Supplemental Executive Retirement Plan (SERP). Pension benefits for SERP participants are intended to cover any benefit reductions that must be imposed for the qualified, defined benefit plan. Eligible retired employees are also provided with postretirement benefits that provide medical, dental, and life insurance. The Company makes periodic contributions to fund the qualified pension plan. The unqualified SERP pension plan and the postretirement benefits are both unfunded.

Incentive compensation or bonus plans have been established for most employees. Key employees, as determined by the Personnel Committee of the Board of Directors, are eligible for the Executive Long-Term Incentive Plan. Employees that directly supervise at least two other employees or otherwise contribute significantly to the Company are eligible for the Executive/Management Incentive Compensation Plan (E/MICP). Other employees not eligible for the above plans are eligible for the Employee Bonus Program or the Marketing Incentive Bonus programs. Amounts paid under the incentive and bonus programs for 2007 were as follows:

<u>Incentive Plan or Program</u>	<u>Plan Year(s)</u>	<u>Eligible Employees</u>	<u>Amount Paid</u>	<u>Average per Employee</u>
Executive Long-Term	2005-2007	29	\$1,991,760	\$68,681
Management Incentive	2007	176	5,713,167	32,461
Employee Bonus Program	2007	827	2,297,193	2,778
Marketing Incentive	2007	34	1,069,756	31,463

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the Missouri Department of Insurance, Financial Institutions and Professional Registration as of December 31, 2007, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 354.075 RSMo (Capital Requirements) and Section 354.410 RSMo (Trust Deposits and Capital Requirements). The funds on deposit, as of December 31, 2007, were as follows:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
U.S. Treasury Notes	\$3,500,000	\$3,577,435	\$3,572,574

Deposits with Other States

BCBS of Kansas City does not have funds on deposit with any other states.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

BCBS of Kansas City is licensed as a Health Services Corporation and as a Health Maintenance Organization in the State of Missouri under Chapter 354 RSMo (Health Service Corporations – Health Maintenance Organizations – Prepaid Dental Plans). The Company is also a licensed insurer in the State of Kansas. The Company's service territory is concentrated in the Kansas City, Missouri metropolitan area and Northwest Missouri, which includes 30 counties in Missouri and 2 counties in Kansas. As of December 31, 2007, total membership was approximately 336,000.

Most of the Company's business is derived from its Preferred Provider Organization (PPO) and HMO products. These products are marketed under various names, depending on the size of the group. Effective May 1, 2006, the Company began transferring its HMO business to its HMO subsidiary, Good Health HMO, Inc. and also began to non-renew policies in the small group and individual markets. With respect to the large group market, the Company intends to discontinue its HMO product by the end of 2009. Effective July 1, 2005, the Company transferred its Medicaid block of business to Blue Advantage Plus of Kansas City, Inc., a newly formed, wholly owned subsidiary.

The Company also provides health insurance through its participation in the Federal Employee Program that is managed by the Blue Cross and Blue Shield Association. The Company also provides a small amount of dental coverage. In addition, the Company has a significant amount of Administrative Services Only (ASO) and Administrative Services Contract (ASC) plan business; for some groups enrolled in ASC coverage, the Company provides stop-loss insurance coverage.

Third-party agents and brokers are utilized to obtain group business. The Company also has a staff of sales and marketing employees that sell and promote its various products. Marketing methods include the use of television, radio, newspaper, and magazine advertisements, billboards, direct mail, and telemarketing.

Policy Forms & Underwriting
Advertising & Sales Materials
Treatment of Policyholders

The DIFP has a market conduct staff that performs a review of the issues listed above, as well as reviews of providers/qualifications, contracts, and marketing initiatives which are documented in a separate market conduct report. The last market conduct exam report issued by the DIFP for BCBS of Kansas City covered the period April 1, 2002 through September 30, 2002 and was issued January 8, 2004. The report resulting from this examination was reviewed and no problems were found that would have a material impact on the Company's financial statements.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

Premiums	2007	2006	2005
Direct premiums written	\$ 832,701,920	\$ 820,999,503	\$ 837,389,263
Reinsurance assumed	12,131,683	12,259,103	10,564,107
Reinsurance ceded	(2,732,614)	(2,316,612)	(1,865,181)
Net premiums written	\$ 842,100,989	\$ 830,941,994	\$ 846,088,189

Assumed

The Company and Healthy Alliance Life Insurance Company (HALIC) entered into a reinsurance agreement effective June 1, 2003. Under the terms of the agreement, BCBS of Kansas City assumes a variable percentage of HALIC's group contracts issued to the Missouri State Teachers Association (MSTA). The Company's assumed percentage of the MSTTA group business is determined by the percentage of MSTTA members located in BCBS of Kansas City's service territory.

Ceded

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

The Company has an excess of loss reinsurance agreement, effective January 1, 1992, with BCS Insurance Company. This agreement covers the Company's PPO, major medical, and stop loss products. The retentions, coverage, limits, and premiums are renegotiated each year and formalized into a schedule signed by both parties. For 2007, the Company's retention was \$500,000 per member per year with a separate aggregate retention of \$800,000 in addition to the per member retention. The reinsurer's specific stop loss maximum liability is \$1.5 million per covered individual per reinsurance period. For 2008, the Company's retention was \$600,000 per member per year with a separate aggregate retention of \$1 million in addition to the per member retention. The reinsurer's specific stop loss maximum liability decreased to \$1.4 million per covered individual per reinsurance period.

BCBS of Kansas City together with its subsidiaries, BA+ and Good Health, are reinsured by an excess of loss agreement, effective January 1, 2008 and terminating on December 31, 2008, with BCS Insurance Company. Services reinsured are those provided to Commercial HMO, Commercial Point-of Services and Medicaid members. The Company's retention is \$600,000 per covered individual per contract period. The reinsurer will reimburse for claims in excess of the retention up to maximum of \$2 million per covered individual per period and \$5 million per lifetime.

BCBS of Kansas City together with its subsidiaries, BA+ and Good Health, are reinsured by an insolvency reinsurance agreement effective January 1, 2007 through December 31, 2007 with BCS Insurance Company. The agreement covers losses incurred in the event BCBS of Kansas City were to become insolvent. The reinsurer's maximum liability is \$5 million per the reinsurance period. The agreement was renewed for the period January 1, 2008 through December 31, 2008 under the same terms.

The Company has a coinsurance agreement, effective December 15, 1998, with General Electric Capital Assurance Company (GECAC) for a long-term care product. BCBS of Kansas City cedes 100% of the risks for the long-term care policies to GECAC.

ACCOUNTS AND RECORDS

Independent Auditor

The CPA firm of Deloitte & Touche, LLP, of Kansas City, Missouri, issued audited statutory financial statements of the Company for the years 2005 and 2006. The CPA firm of Ernst & Young, LLP, of Kansas City, Missouri, issued audited statutory financial statements of the Company for 2007.

Independent Actuary

The 2005 and 2006 actuarial items reported by the Company were certified by David O. Thoen, FSA, MAAA, of Deloitte Consulting, LLP, of Minneapolis, Minnesota. The 2007 actuarial items reported by the Company were certified by Darrell D. Knapp, FSA, MAAA of Ernst & Young, LLP, of Kansas City, Missouri.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of BCBS of Kansas City for the period ending December 31, 2007. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore were only communicated to the Company and noted in the workpapers for each individual Annual Statement item.

Assets

	Ledger and Non-Ledger Assets	Assets Not Admitted	Net Admitted Assets
Bonds	\$ 266,969,462	\$ -	\$ 266,969,462
Preferred stocks	714,492	-	714,492
Common stocks	261,788,357	4,712,447	257,075,910
Properties occupied by company	24,878,009	-	24,878,009
Cash, cash equivalents and short-term investments	15,998,372	-	15,998,372
Other invested assets	11,143,959	11,143,959	-
Receivables for securities	805,195	-	805,195
Investment income due and accrued	2,629,765	-	2,629,765
Uncollected premiums and agents' balances	13,821,050	-	13,821,050
Amounts recoverable from reinsurers	1,355,000	-	1,355,000
Amounts receivable relating to uninsured plans	38,000,391	185,000	37,815,391
Current federal income tax recoverable	31,536,792	-	31,536,792
Net deferred tax asset	22,098,985	12,247,856	9,851,129
EDP equipment and software	17,388,251	11,625,691	5,762,560
Furniture and equipment	2,104,152	2,104,152	-
Receivable from parent, subsidiaries and affiliates	7,283,512	1,645,716	5,637,796
Healthcare and other amounts receivable	32,955,604	1,028,684	31,926,920
Aggregate write-ins for other assets:			
Prepaid pension benefit cost	32,858,506	32,858,506	-
Prepaid expenses	6,903,537	6,903,537	-
Other assets non-admitted	7,049,350	7,049,350	-
Intangible SERP asset	465,747	-	465,747
Total Assets	\$ 798,748,488	\$ 91,504,898	\$ 707,243,590

Liabilities, Capital and Surplus

Claims unpaid	\$ 101,621,107
Accrued medical incentive pool and bonus amounts	198,588
Unpaid claims adjustment expenses	4,908,680
Aggregate health policy reserves	10,864,709
Aggregate health claim reserves	625,656
Premiums received in advance	31,505,202
General expenses due or accrued	30,609,565
Ceded reinsurance premiums payable	230
Amounts withheld or retained for account of others	1,708,495
Remittance and items not allocated	2,161,080
Amounts due to parent, subsidiaries and affiliates	3,725,411
Payable for securities	583,256
Liability for amounts held under uninsured plans	793,664
Aggregate write-ins for other liabilities:	
Unfunded post-retirement benefit obligation	35,207,000
Deferred loss on operating lease	20,364
Accrued supplemental retirement plan liability	13,199,666
Uncashed check pending escheatment	1,452,912
Other	281,716
Total Liabilities	239,467,301
Statutory reserve	1,000,000
Unassigned funds (surplus)	466,776,289
Total Capital and Surplus	467,776,289
Total Liabilities and Capital and Surplus	\$ 707,243,590

Statement of Revenue and Expenses

Net premium income	\$ 842,100,990
Change in unearned premium reserve for rate credits	<u>79,714</u>
Total revenues	842,180,704
Hospital and Medical:	
Hospital/medical benefits	602,175,288
Emergency room and out-of-area	14,045,644
Prescription drugs	79,124,979
Incentive pool, withhold adjustments and bonus amounts	359,576
Net reinsurance recoveries	<u>9,227,083</u>
Total hospital and medical	704,932,570
Claims adjustment expense	35,049,378
General administrative expenses	75,468,425
Increase in reserves for life and accident and health contracts	<u>2,669,108</u>
Total underwriting deductions	818,119,481
Net underwriting gain or (loss)	24,061,223
Net investment income earned	26,759,139
Net investment gains (losses)	<u>11,566,155</u>
Net investment gains (losses)	\$ 38,325,294
Embossed card revenue	286,363
Intercompany interest	<u>362,876</u>
Aggregate write-ins for other income or expenses	\$ 649,239
Net income or (loss) before income taxes	63,035,756
Federal income taxes incurred	<u>(28,394,658)</u>
Net income or (loss)	<u>\$ 91,430,414</u>

Capital and Surplus Account

Capital and Surplus, December 31, 2006	\$ 375,138,391
Net income	\$ 91,430,414
Change in unrealized capital gains	(1,419,703)
Change in net deferred income tax	(1,361,147)
Change in nonadmitted assets	4,235,493
Aggregate write-ins for gains or (losses) in surplus:	
Change in additional minimum supplemental retirement	(40,445)
Change in negative net worth of subsidiary	(206,716)
	<hr/>
Net change in Capital and Surplus for the year	<hr/> <hr/> 92,637,896
Capital and surplus, December 31, 2007	\$ 467,776,287

Notes to the Financial Statements

None.

Examination Changes

None.

General Comments and/or Recommendations**Agreement for the Management of Intercompany Payables and Receivables (page 14)**

The Agreement for the Management of Intercompany Payables and Receivables contradicts the Medicaid Agreement between BA+ and the State of Missouri. The Medicaid Agreement requires direct payment of premiums to BA+'s bank account while the Agreement for the Management of Intercompany Payables and Receivables gives BCBS of Kansas City the authority to collect all premiums. The Company is directed to amend the Agreement for the Management of Intercompany Payables and Receivables to exclude the Medicaid premium portion paid directly to BA+ from BCBS of Kansas City's authority to receive the subsidiary's remaining receivables. The amendment should be filed with DIFP in accordance with Section 382.195 RSMo (Prohibited transactions, exceptions).

Administrative Agreement with EPOCH (page 14)

As part of its move into a separate office building, EPOCH is reimbursing BCBS of Kansas City for certain administrative expenses. The reimbursement of these expenses is not addressed in the Administration Agreement. The Company should amend the current Administration Agreement to include the expense reimbursements or enter into a separate agreement with EPOCH that address the reimbursements. The amendment or new agreement should be filed with the DIPF as required by Section 382.195 RSMo (Prohibited Transactions, Exceptions).

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Blue Cross and Blue Shield of Kansas City during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Bernie Troop, CFE, Alvin Garon, CFE, Leslie Nehring, CPA, CFE, Karen Baldree, CFE, CPA, Steven Koonse, CFE and Angi Campbell, CFE, AES, examiners for the Missouri Department of Insurance, Financial Institutions and Professional Registration participated in this examination. In addition, Bertram Oparaji, CFE, representing the Kansas Department of Insurance also participated in the examination. The firm of Milliman, Inc., of St. Louis, Missouri participated as a consulting actuary.

VERIFICATION


State of Missouri)
)
 County of)

I, Mark Nance, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Blue Cross and Blue Shield of Kansas City, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.



Mark Nance, CPA, CFE
 Examiner-In-Charge
 Missouri Department of Insurance, Financial Institutions
 and Professional Registration

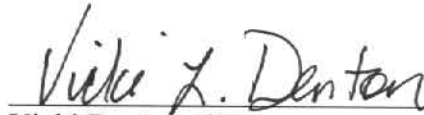
Sworn to and subscribed before me this 6th day of November, 2008.

My commission expires: 04/14/2012 
 Notary Public

BEVERLY M. WEBB
 Notary Public - Notary Seal
 STATE OF MISSOURI
 County of Clay
 My Commission Expires 4/14/2012
 Commission # 08464070

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

A handwritten signature in cursive script, reading "Vicki L. Denton". The signature is written in dark ink and is positioned above a horizontal line.

Vicki Denton, CFE

Audit Manager

Missouri Department of Insurance, Financial Institutions
and Professional Registration



BlueCross BlueShield of Kansas City

An Independent Licensee of the
Blue Cross and Blue Shield Association

One Pershing Square
2501 Main
P.O. Box 419169
Kansas City, MO 64141-6169
Telephone: 816-395-2222
www.bcbskc.com

December 19, 2008



Mr. Frederick Heese, CFE, CPA
Chief Financial Examiner &
Acting Division Director
Missouri Department of Insurance
PO Box 690
Jefferson City, MO 65102-0690

Re: Response to Exam: Blue Cross Blue Shield of Kansas City

Dear Mr. Heese:

This letter is in response to your letter of November 25, 2008 requesting verification of compliance with the comments and recommendations from the financial examination for the Company as of December 31, 2004. We request that our response be included in the report as a public document.

- Agreement for the Management of Intercompany Payables and Receivables

We will amend this agreement to exclude the Medicaid premium paid directly to BA+ and will file the amendment with DIFP.

- Administrative Agreement with EPOCH

We will amend the Administrative Agreement with EPOCH and will file the amendment with the DIFP.

If after reading the responses you have additional questions, you can reach me at 816-395-2750, or by e-mail at marilyn.tromans@bcbskc.com.

Sincerely,

Marilyn Tromans
Vice President, CFO